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Governing Markets in Gulf States

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Abstract
Gulf states have altered the institutions of market governance as part of new strategies to develop their domestic markets and attract outside investment. In a sharp break from traditional institutions, several states have created new sectoral independent regulatory agencies (IRAs) in key sectors. The paper examines when, how and why these agencies have been created in two economically and politically strategic sectors – stock exchanges for company securities trading and telecommunications – that lie at the heart of new economic strategies. It argues that an analytical framework based on internationalization best explains the pattern of partial adoption of IRAs in Gulf Cooperation Council (GCC) states. International factors have provided crucial impetus for reform. The desire to attract non-Gulf capital and expertise has provided a rationale for IRAs; overseas reforms have offered examples to be copied or at least modelled; the recommendations of international organizations and free trade agreements have aided in legitimating reforms. But the impact of international factors has been mediated by domestic conditions, including the extent of oil wealth and the position and strategies of national policymakers. As a result, the spread of IRAs varies significantly among GCC states.

1. INTRODUCTION

Since the 1990s several Gulf states[1] have sharply altered the governance of their markets by adopting institutions widely used in other countries, notably the United States and Western Europe. They have ended legal monopolies, established rules for competition and delegated powers to regulatory agencies. The spread of such institutions is a puzzle: why should Gulf Cooperation Council (GCC) countries, despite their considerable wealth, adopt reforms that run counter to their traditional market and governmental institutions?

This paper examines the institution of market governance in two sectors – stock exchanges for company securities trading and telecommunications. More specifically, it focuses on analyses of when, how and why Gulf states have created 'independent regulatory agencies' (IRAs). IRAs are a fascinating example of wider changes in the governance of Gulf markets: they represent a clear institutional break with the past; they are an importation from abroad; they are closely linked to other policies of reforming domestic markets such as liberalization, adoption of

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[1] Gulf states referred to here are the Gulf Cooperation Council (GCC) member states: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates.

international standards and privatization. Moreover, regulatory agencies form part of current discussions over the regulation of complex and large markets, especially in finance.

Stock exchanges and telecommunications are chosen for three reasons. First, they are economically and politically strategic sectors. Second, they lie at the heart of new strategies by GCC states of attracting inward investment and developing domestic markets, both directly and through their linkage to other sectors such as banking, tourism and information technology. Indeed, they offer a form of 'critical case' for the extent of change in market governance institutions in the Gulf because they are the most likely sectors to experience reform. Third, IRAs have spread in these two sectors across several Gulf states in recent years or are the subject of current debate, revealing the forces and constraints that shape change.

There follows a short overview of the context of market governance and the spread of agencies in securities trading and telecommunications in Gulf states. The paper then introduces theoretical analyses by setting out three broad interpretations of changes in governance: national choice based on a principal–agent model, cross-national diffusion of institutions, and an internationalization approach focusing on the interaction between international factors and domestic policy processes. Thereafter it looks in detail at the creation of agencies for stock exchanges and telecommunications. The conclusion offers some wider discussion about changes and challenges in the governance of markets in GCC states.

The central argument is that IRAs have spread in telecommunications and stock exchanges in GCC countries. But also they have spread unevenly, with some states not adopting them or only creating agencies that lack sufficient formal or legal independence from governments to qualify as IRAs. This pattern of the partial adoption of formal Western institutions is best explained by an internationalization model that involves interactions between specific international forces and domestic factors. The key international forces have been the desire to attract non-GCC investment and expertise, cross-national learning and 'modelling' from overseas institutions from outside the Gulf. However, domestic factors have been central for whether, when and how such learning and modelling takes place and their institutional impacts. Thus IRAs have been created when national policymakers, notably unelected rulers, have developed focused strategies, often because they feared a lack of energy wealth and were very keen to attract inward investment. There is a paradox that strong leadership by unelected rulers can aid swift change whereas stronger, more independent legislatures can limit new institutions. Equally, high energy reserves can limit the perceived need for reforms. Hence international factors have been crucial for the spread of IRAs, but their impacts also depend on domestic conditions.

The paper focuses on decisions to create IRAs. It does not look at their performance or their effects on economic outcomes, which would require a separate paper. The very sharp change in institutions governing markets is in itself an important political and governmental phenomenon to be explained and understood before looking at subsequent developments.

2. OVERVIEW OF MARKET GOVERNANCE AND THE SPREAD OF AGENCIES

The states of the Gulf enjoy many economic advantages, notably high levels of wealth thanks to oil and gas. But they also face strong challenges (for an excellent analysis see Shochat, 2008). Their populations are growing rapidly. Oil and gas prices are highly volatile. Overseas investment by GCC states has met resistance, demands for reciprocal access to Gulf markets and pressure for the adoption of 'international' regulatory standards. Their security is uncertain.

At the same time, important differences among GCC states should be noted. Several states have limited energy reserves (notably Bahrain and Dubai), while others have plentiful oil and gas supplies and hence face much less need to develop non-oil industries (especially Kuwait, Abu Dhabi, Qatar and Saudi Arabia). The nature of wider government reforms also shows variation. Thus, for instance, Kuwait's parliament is seen as one of the most independent and powerful, with contested elections, and Dubai has sought to adopt Western institutions, whereas Saudi Arabia has retained more traditional approaches to government.

In response to economic, political and security challenges, Gulf states have adopted radically new economic strategies since the 1990s, although the extent and timing of change have differed across countries. One part of that strategy involves building companies with major overseas stakes, both through national companies expanding abroad and through sovereign wealth funds; such expansion is not the subject of this paper, but is an important factor insofar as altering domestic markets is seen as a quid pro quo for overseas expansion by domestic companies.

The other part of GCC economic strategies is the development of domestic markets and companies through the entry of overseas firms both as suppliers and investors. Very importantly, 'internationalization' primarily refers to the world outside the Gulf – interviewees emphasized that they were focusing on non-Gulf investors. It has been seen most clearly in telecommunications and stock exchanges, but also to a lesser extent in banking and infrastructure development and sometimes even in the core energy sectors.

A key part of attracting non-GCC investors has been the adoption of Western formal institutions and rules. One element has been liberalization – that is, ending legal monopolies and rules restricting inward investment. Another has been corporatization, as existing telecommunications companies have been transformed into quoted companies, and sometimes privatization. But a third, key, element has been the creation of IRAs.

IRAs have been seen as offering a number of advantages for attracting inward investment from outside the Gulf, especially in stock exchanges and telecommunications. They are claimed to offer reassurance to investors that they will be treated fairly, notably compared with local investors. This is crucial in telecommunications, in which there are heavy sunk investments, and also in stock markets, where investors worry about insiders who may enjoy privileged information and treatment. IRAs may set clear predictable rules so that investors can plan for the long term. Equally, they are designed to set rules to govern liberalized markets in ways that allow new entrants to compete fairly with incumbents. Enhanced efficiency is another aim of IRAs, as policymakers seek organizations that can recruit the best personnel on the basis of merit, including from abroad. More generally, it has been hoped that IRAs may be able to resist short-term pressures from governments and domestic interests, and instead will follow longer-term policies based on clear principles.

Given that many regulatory bodies can be called independent, it is important to define and set minimum conditions for IRAs. An IRA is a regulatory organization separated from government ministries and from suppliers. It can be defined as a body given powers under public law, whose head has a degree of tenure and which has its own organizational resources. These minimum institutional features mean that, in formal institutional or legal terms, IRAs enjoy provide a degree of independence both from governments, which cannot simply dismiss the head of an IRA or remove its resources, and from suppliers, who face a body with its own legal and organizational resources.[2] Not all agencies are IRAs – it is possible to have specialized regulatory agencies that lack the formal institutional or legal independence from governments to qualify. It is also crucial to note that these institutional features refer to the formal institutional independence of IRAs from governments – which is distinct from their independence in practice from both governments and regulated interests. This paper examines the creation of formally independent agencies.

Table 1 summarizes the spread of IRAs in securities trading across GCC states. Hence it examines whether an IRA has been established, the date of its creation, and its key institutional features. Within the United Arab Emirates (UAE) it also examines the two largest emirates, Abu Dhabi and Dubai, as stock exchange regulators have also been set up at the emirate level. The table shows that three states (Dubai, Qatar and Saudi Arabia) have created fully fledged IRAs. Kuwait is actively discussing an IRA. However, three states have followed alternative institutional reforms – the UAE and Oman, which have agencies that lack sufficient formal independence to qualify as an IRA, and Bahrain, which has given regulatory functions to the central bank.

Table 1. IRAs for stock markets in GCC states

GCC country	**IRA**	**Date created**	**Key institutional features**
Bahrain	No: the central bank (Bahrain Monetary Agency) is the regulator.		
Kuwait	Under discussion – planned for 2008.		
Oman	No: the Capital Market Authority (CMA), established in 1998, is a government authority responsible for organizing and overseeing the issue and trading of securities in the Sultanate.		

[2] Thereafter the degree of formal independence is a variable, depending on many factors, ranging from powers of reappointment to length of term and continuing government controls. See Thatcher and Stone Sweet (2002), Gilardi (2002).

GCC country	IRA	Date created	Key institutional features
Qatar	Qatar Financial Centre Regulatory Authority (QFC).	2005: QFC Law (Law No. 7 of 2005) was signed by the Emir of the State of Qatar on 9 March 2005 and became effective on 1 May 2005.	Regulates financial services firms that conduct regulated activities in, or from, the QFC. Has an appeal body, the QFC Regulatory Tribunal. Plan to have unified financial regulator overseeing banking and securities by 2008/2010.[3]
Saudi Arabia	Capital Market Authority – ‘government organization with financial, legal and administrative independence. It reports directly to the Prime Minister.’	2003: The Capital Market Law (CML) was issued by Royal Decree number m/3 dated 31/7/2003.	Board composed of five members, who shall be natural Saudi Arabian persons. Financial budget submitted to ministry of finance.
UAE federal level	Emirates Securities and Commodities Authority – although it has a legal personality it is not an IRA because it is headed by representatives of ministries.	2000: Federal Law No. 4 of 2000 concerning the Emirates Securities and Commodities Authority and Market.	Regulates UAE domestic securities market, e.g. Abu Dhabi securities market and Dubai financial market.
Dubai	Dubai Financial Services Authority (DFSA).	Dubai Law No. 9 of 2004, The Law Establishing the Dubai International Financial Centre.	Regulates the international market, Dubai International Financial Centre (DIFC), including Dubai International Financial Exchange (DIFX), acting under a separate legal system.

Table 2 summarizes the spread of IRAs in telecommunications across GCC states. It shows that two states (Bahrain and the UAE) have created specialized agencies that can qualify as IRAs. Of these, the most formally independent is the

[3] See *Financial Times*, 17 July 2007.

Telecommunications Regulatory Authority (TRA) in Bahrain. Three other states (Oman, Qatar and Saudi Arabia) have also set up sectoral agencies, but because of the powers that remain in the hands of ministers, they do not have sufficient legal independence to qualify as fully fledged IRAs.

Table 2. IRAs in telecommunications

GCC country	Sectoral IRA	Date created	Key institutional features
Bahrain	Telecommunications Regulatory Authority (TRA).	2002.	Strong formal independence, e.g. powers vested in General Director, appointed for one term, but this is renewable and General Director is difficult to dismiss.
Kuwait	Under discussion – planned for 2008; at present the regulator is ministry of posts and telecommunications.		
Oman	No: Sultanate of Oman Telecommunications Regulatory Authority is chaired by a minister.	2002	Three full-time members but chaired by minister of transport and communications
Qatar	No: ictQATAR.	2004 and 2006: a 2004 emiri decree gave ictQATAR the authority to regulate the country's telecommunications market. Decree Law Number 34 of 2006 gives ictQATAR a full range of powers to regulate the telecommunications market in Qatar.	ictQatar headed by the Supreme Council for Communication and Information Technology, chaired by the minister.
Saudi Arabia	No: a sectoral body, the Communications and Information Technology Commission (originally	2001 Telecoms law.	The Commission's Board is chaired by the minister, and membership includes 'representatives'

GCC country	Sectoral IRA	Date created	Key institutional features
	called Saudi Communications Commission), lacks sufficient independence to qualify as an IRA.		from the ministries of the ministry of PTT, the ministry of finance and national economy, and the ministry of commerce.
UAE federal level	Telecommunications Regulatory Authority (TRA) of the United Arab Emirates.	UAE Federal Law by Decree No. 3 of 2003, Telecom Law.	Managed by a board of directors, comprising five board members, including the chairman and the Director General. The Board is appointed by resolution of the Supreme Committee for a period of four years renewed for similar periods; its dismissal is only possible on grounds stated in the law.

Overall, the tables show a remarkable spread of specialized sectoral agencies across most Gulf states in both telecommunications and securities trading. Several of these agencies enjoy substantial legal independence from governments and can be qualified as IRAs, but others do not, notably because government ministers chair or sit on their boards.

The decision to create IRAs calls for analysis and explanation because they mark a sharp break with the general government and political structure of GCC states. Establishing IRAs involves the legal separation of public agencies from governments by formal delegation of powers and the setting out of explicit statutory objectives and powers. Yet most GCC states have relatively small populations, are led by major families and hereditary rulers and have traditions of informal consultation or much interlinkage between society and state. Indeed, Gulf states have no administrative or political tradition of IRAs or similar structures, in contrast, for instance, to the United States, which had regulatory commissions dating from the late nineteenth century, or

Britain, which had parliamentary commissions in the nineteenth century. Hence creating new structures based on transferring powers, formality and the separation of an agency from the state and society is a real innovation for GCC states.

The creation of IRAs is also surprising given the history of telecommunications markets and stock markets in Gulf states until the 1990s. Both sectors were small and had few services. They were regulated by traditional institutions, notably government ministries and, sometimes, associations of suppliers. They were publicly owned and largely inward-looking, towards the domestic or GCC market. The role of non-GCC suppliers and investors was very small.

At the same time the spread of IRAs in stock exchanges and telecommunications has been uneven among GCC states: some countries have not (yet) established IRAs, while others have created specialized agencies that are closely linked to governments, such as those in Saudi Arabia. This suggests that the ease or difficulty of establishing IRAs and/or the desire for IRAs varies, reflecting contrasts both in wider government structures and in economic strategies.

Explaining why IRAs have been established (and sometimes why they have not been created) calls for theoretical tools to guide empirical study.

3. Analytical frameworks for studying the spread of IRAs

Reform of market governance and the spread of IRAs have been studied both in Europe and elsewhere.[4] Among the diverse literature, three analytical frameworks have emerged that offer well-developed explanations relevant for GCC states: a national model of delegation based on principal–agent explanations; an international diffusion model; and an internationalization model based on the interaction of international and domestic factors.

The national delegation approach suggests that national policymakers choose to establish IRAs following a rational calculation of the costs and benefits of delegation.[5] Creating IRAs takes resources of time and money; moreover, policymakers are handing over powers to IRAs, which may use them in ways undesired by the former, leading to ‘agency losses’. But IRAs can bring advantages for national governments and politicians. The literature often underlines economic

[4] For the spread of IRAs see Thatcher (2002), Levi-Faur (2003) and Gilardi (2005).

[5] This is based on principal–agent theory; for reviews in political science see, e.g., McCubbins (1985), Calvert, McCubbins and Weingast (1989), Huber and Shipan (2000), Bendor, Glazer and Hammond (2001) and, more generally, Epstein and O’Halloran (1999).

advantages. A key benefit for developing countries is argued to be enhanced ‘credible commitment’, that helps to reassure investors, especially overseas ones, that if they sink their investments now, future returns on those investments will not be taken away by government intervention (cf. Levy and Spiller, 1996). Investor fears are a particular problem in industries such as telecommunications and in securities trading; in the former, large sunk costs are often required for new networks, while in the latter investors fear sudden changes such as exchange-rate restrictions, new taxes, unfair market advantages for privileged actors or the suspension of ordinary trading rules in periods of market turbulence. It is also important in countries with histories of unpredictable regulatory changes. Since IRAs are separate from the government and are given explicit duties and powers, they offer a means of enhancing the credibility of promises to investors about future regulation.

Policymakers may also choose to delegate powers to IRAs in order to achieve higher regulatory efficiency to deal with increased technical complexity; a specialized organization may be better placed to develop expertise than, for instance, a government department. Regulatory complexity increases both with technological change and with liberalization, which usually requires setting rules to deal with competition. Both stock markets and telecommunications have become much more complex, because of both technological change and liberalization. Finally, policymakers may also choose to create IRAs to shift blame for unpopular decisions or to deal with international organizations which make rule-making more complex or which limit the discretion of national governments and hence their ability to use regulation in ways that benefit them.

The second approach is to look at the international diffusion of institutions. It suggests that, since states are interlinked, decisions in one country affect and are affected by prior decisions in other states, sometimes transmitted or mediated by international organizations. As a result, similar institutions can spread across very diverse states, leading to the international diffusion of institutions. Hence it has been claimed that in the past decades there has been the diffusion of ‘liberal’ economic institutions across the world (Simmons and Elkins, 2004; Simmons, Dobbin and Garrett, 2006).

There are several possible mechanisms for the transnational diffusion of neo-liberal institutions. It may occur through coercion, be this through legal requirements and conditions set by international organizations or through manipulation of costs and benefits as dominant countries affect the incentives of others or set international norms. In both telecommunications and securities trading, powerful states which are responsible for large shares of the world market (notably the United States and many EU countries) have adopted IRAs. Equally, international organizations such as the World Trade Organization (WTO), the International Organization of Securities Commissions (IOSCO), the International Monetary Fund (IMF) and the World Bank have clear policies favouring IRAs and can make membership or loans dependent on adherence to their policies.

‘Regulatory competition’ can also result in diffusion, as rival states alter their domestic institutions to make themselves more attractive to international investors and companies (see Radaelli, 2007). If a country fails to match them, it risks losing out. In stock exchanges and telecommunications, IRAs can form part of strategies to attract international investors by the promise of better-quality regulation. Learning offers a third mechanism for diffusion, as countries may look to the experiences of others and draw lessons (see Bennett, 1991; Rose, 1993; Campbell, 1998). A fourth and closely related mechanism can be emulation or ‘modelling’, when countries follow global norms of ‘best practice’ regarding institutions, even though they cannot evaluate the costs and benefits of those institutions, which in fact may not be appropriate for their domestic circumstances. (cf. Braithwaite and Drahos, 2000; McNamera, 2002). Since IRAs for telecommunications and securities have been adopted in many countries, notably in western Europe, the third and fourth mechanisms would mean that other countries follow the example of these ‘policy leaders’. Indeed, sociological versions of the diffusion model argue that countries adopt overseas examples regardless of whether those examples are appropriate or increase efficiency (cf. McNamera 2002). Hence they would claim that IRAs, which were developed in Western states, are imported into other political and administrative systems even if they do not in fact offer the benefits that the principal–agent model suggests they should.

The third analytical approach is an ‘internationalization’ analysis, based on the ‘second image reversed’ (see Gourevitch, 1978 and Katzenstein, 1978). It focuses on how and why international factors enter and are used in the domestic policy process. Early work examined how changes in the costs and benefits of cross-border economic exchanges, notably cross-border trade, affected incentives to alter domestic policies (see Milner, 1988; Milner and Keohane, 1996; Frieden and Rogowski, 1996). More recent studies have argued that ‘policy forms’ of internationalization can also be crucial, such as the policies and institutions of powerful overseas nations or supra-national regulation (Thatcher, 2007). Hence they suggest that economic costs and benefits are not the only form of international influence on domestic decisions. They also point to the vital role of international factors in the political process – especially in providing impetus for national policymakers to alter their strategies and in creating new reform coalitions and overcoming opposition.

The internationalization literature claims that responses to internationalization are strongly influenced by domestic factors as international factors become enmeshed in national politics. They can offer national policymakers opportunities to legitimize institutional reforms, but also margins of choice, as they can interpret and use overseas experiences, giving rise to differences in processes of reform, strategies and/or outcomes (Katzenstein, 1985; Gourevitch, 1986; Hallerberg and Basinger, 1998; Thatcher, 2007).

Thus an internationalization approach suggests that analysis of the spread of IRAs should focus on how altered international factors modify the incentives, resources and coalitions of policymakers within the domestic policymaking process. It points to the increasing internationalization of both securities trading and telecommunications markets as likely to affect reform of domestic institutions through higher cross-border exchanges, the potential for international regulatory competition and cross-national policy learning and modelling due to reforms in different states, and the expansion of supranational regulation.

The literature on delegation, international diffusion and internationalization can be used to generate three sets of propositions regarding the spread of IRAs and explanatory factors and processes. The first, based on the delegation model, points to the national context and suggests that national policymakers carefully weigh up the costs and benefits of delegating to IRAs and then choose whether or not to do so. If they create IRAs it is because of the benefits that IRAs bring them, notably enhancing credible commitment, responding to increased complexity, shifting blame for unpopular decisions and dealing with international organizations. This approach implies that several of the stated reasons for creating IRAs in GCC states discussed above in section 2 are in fact sufficient to explain their spread – that is, IRAs have been adopted because they perform useful functions for national policymakers, such as attracting inward investment thanks to enhanced credible commitment and more efficient regulation. At the same time, it predicts that if national circumstances and institutions vary so that they affect the need for IRAs and/or the benefits of IRAs for national policymakers, there will also be significant variations in the spread of IRAs across countries.

The second literature, on policy diffusion, locates the impetus for delegation in the international environment and suggests that national policymakers are strongly influenced by overseas decisions. Indeed, it implies limited choice for countries which are swept along in international institutional reform waves through processes such as coercion, competition with the cross-national learning of other states and emulation. An international diffusion approach would predict that similar institutions spread across GCC states despite domestic differences, as national policymakers are forced into adopting IRAs or in fact learn or copy overseas examples regardless of differences in their domestic institutions and circumstances.

The third literature, on internationalization, argues that international factors (which can be technological and economic but also the policies of other countries and supranational regulation) are crucial for decisions on institutional reforms through their effects on the domestic policy process. They provide impetus for reform by altering the incentives, opportunities, strategies, coalitions and legitimizing arguments of national policymakers to reform institutions. Hence it would suggest that overseas factors have been central in GCC states' deciding to create IRAs, especially by aiding reformers and weakening their opponents. But, in contrast to the diffusion literature, it examines the interaction of those factors with domestic policymaking and institutions that mediate and mould responses to the international forces for change. Thus it predicts considerable differences in the effects of international factors and also in outcomes if domestic conditions also vary.

The three literatures are valuable in providing factors and mechanisms to look for. Analysing the factors suggested by the three models requires detailed process-tracing and consideration of the empirical evidence. Given industry differences, stock exchanges and telecommunications are analysed separately.

3.1. The spread of IRAs for securities trading in Gulf states

Until the 1980s there were no formal stock exchanges in GCC countries. Instead, very small informal over-the-counter markets existed, often in shops or markets. They were largely unregulated, or at most were supervised by associations of traders. Attempts were made in the 1980s to expand stock markets in order to aid the private sector and reduce dependence on governments.[6] In particular, the official Kuwait Stock Exchange was established after the 1982 Al-Manakh crash involving the existing over-the-counter market, the Bahrain stock exchange was set up in 1987 and the Oman exchange in 1989 (World Bank, 2004).[7] The stock markets were usually publicly owned. Often they were 'regulated' through broadly drafted laws and very loose rules drawn up and enforced either by the central bank (e.g. Bahrain after 1987) or by a combination of the finance ministry and 'self regulation' by an association of traders (e.g. the Kuwait Stock Exchange). Trading was very limited in volume.[8] Stocks were domestic; insofar as overseas stocks were traded, they were for firms from neighbouring Gulf states. Often trading was dominated by shares in government-owned companies, largely because most privately owned companies were family owned. There were very few rules governing trading – for instance, insider trading was not an offence. Moreover, stock exchanges suffered from problems involving speculation, insider trading and sudden price rises and falls (see, e.g., *Financial Times*, 4 December 2000). In addition, the 1990 invasion of Kuwait greatly damaged the Kuwait Stock Exchange, which had been the oldest and largest in the Gulf.

The period from the late 1990s onwards saw pressures and opportunities for change in stock exchanges. Wealth is concentrated, and much is held outside the region.[9] However, obstacles to investment and transfers of funds in Western countries emerged, with much greater suspicion of Islamic banks, especially after 9/11, giving incentives to find regional opportunities for Gulf investors.[10] At the same time, private companies faced difficulties raising finance from local stock markets, and were highly dependent on governments or banks or otherwise international financial markets, which in turn demanded state guarantees.[11] Other Arab states began to seek to develop stock markets with IRAs in order to attract capital, offering regulatory competition to GCC states; in particular, Jordan set up an IRA for securities in

[6] For an analysis see *Financial Times*, 12 July 1988.

[7] For Oman see Allen and Rigsby (2000); for background analysis see *Financial Times*, 12 July 1988.

[8] One estimate was that the Dubai OTC market had c. 26 listed securities before 2000 and trading amounted to a few thousand dirham (interviewee 10).

[9] One estimate is that in 1998 the 350,000 wealthiest Gulf nationals, representing 2 per cent of the region's population, owned US$800 billion of assets, half of which were held abroad (*Financial Times*, 26 March 1998).

[10] See e.g. claims that Islamic banks 'funded extremist organizations' (*Financial Times*, 21 Oct. 2001).

[11] For instance, in 1998 the state-owned Saudi Arabian Airlines failed to raise US$4.5 billion capital from local stock markets and found that international markets demanded a sovereign guarantee (*Financial Times*, 26 March 1998).

1997.[12] Meanwhile, a major boom in GCC stock markets during the late 1990s and early 2000s, due to loose credit provided by banks (which also profited from share sales), was followed by a major downturn in 2005–6 that led to large losses for investors, with many markets falling by 25–50 per cent (cf. *Middle East Economic Digest*, 24 November 2006, p. 88).[13] Strong discontent arose over the lack of rules on matters such as insider trading, with public demonstrations in some countries (interviews; *La Tribune*, 15 March 2006).

In this new context, Gulf states began to reform their stock markets.[14] They sought to develop alternative sources of investment for citizens and finance for firms. But several also aimed to attract non-GCC capital to build up a strong international financial sector, with attendant revenues, employment and growth. The earliest and most far-reaching reforms were in Dubai. Lacking large oil revenues, it has sought to develop itself as a hub or international or 'world city', with high-class infrastructure – an international airport, a first-class airline, tourist attractions, spectacular new buildings and tax-free zones (cf. Marchal, 2001, and Davidson, 2007). In the field of finance it created the Dubai International Financial Centre (DIFC), initially launched in 2002 and then legally established in 2004.[15] This followed a change in the UAE (federal) constitution in 2004 to allow individual emirates to establish free trade zones.[16]

The initiative to create the DIFC was taken by the then Crown Prince His Highness Sheikh Mohammed Bin Rashid Al Maktoum (now Emir of Dubai) (interviewees 9 and 10). It formed part of an overall strategy of developing and diversifying Dubai in response to its lack of oil (interviewees 10 and 12). The ambition was to create a regional financial centre, using a time zone between those of Tokyo, London and New York, aimed at international investors from outside the GCC countries (interviewees 10 and 12).

The creation of the DIFC involved substantial changes in regulation. A separate stock market – the Dubai International Financial Exchange (DIFX) – was

[12] The Jordan Securities Commission, created by Securities Law, No. 23, 1997.
[13] For instance, the Tadawul all-share index for the Saudi Arabian stock market fell 52.5 per cent in 2006 (*La Tribune*, 30 Jan. 2007).
[14] For data on stock market sizes, see Appendix and also Shochat (2008).
[15] UAE Federal Decree No. 35 of 2004, establishing the DIFC as a financial free zone in Dubai Middle East, and Dubai Law No. 9 of 2004, The Law Establishing the Dubai International Financial Centre; for a discussion see *Middle East Economic Digest* (10 Jan. 2004, p. 8).
[16] Federal Law No. 8 of 2004, Regarding the Free Trade Zones.

established for international investors and stock. The DIFX is regulated by an IRA established specifically for the purpose, namely the Dubai Financial Service Authority (DFSA).[17] In contrast the existing local exchange, the Dubai Financial Market (formally established in 2000)[18] remained a domestic market regulated by the Emirates Securities and Commodities Authority (ESCA), whose board is chaired by the minister of finance and commerce and hence is not sufficiently legally separate from the government to be an IRA.[19] Moreover, Dubai has established an international financial and legal ‘island’ to attract overseas investors and trading. Almost all dealing within the DIFC were exempt from UAE civil law. Instead, special legislation was passed to create a judicial system for the DIFC largely based on the Anglo-Saxon legal system, under the DIFC Judicial Authority.

The DFSA was created to help attract international capital and to ensure high standards of corporate governance (Interviewees 9 and 12). It followed a study in 2001–2 by, the consultant group McKinsey that argued for a special financial services regulator. In addition, policymakers wished to meet the principles of IOSCO, which state that ‘The regulator should be operationally independent and accountable in the exercise of its functions and powers’ (IOSCO, 2003; interviewee 8). The Crown Prince and his advisors looked at overseas examples, notably Britain, the United States and Hong Kong (interviewees 10 and 12). But the British Financial Services Authority (FSA) was the ‘primary model’ for the DFSA (interviewee 9). Indeed, the DFSA was largely planned by Philip Thorne, a former managing director of the FSA, and Ian Hay Davidson, former managing director of Lloyds of London, who became respectively its chief executive and chairman. There was little opposition to the idea of a separate regulator within Dubai, in large measure because the DIFC was an international zone with a separate market for regional players; only business parts of the DIFC expressed some opposition, being used to conducting business in a traditional manner (interviewee 9). The creation of an IRA with substantial legal independence from far from easy, however. In June 2004 Thorpe and Hay-Davidson were dismissed from their posts at the DFSA. Reported reasons included their desire to create an IRA that was independent from the DIFC and the application of rules to

[17] In 2007 a holding company, Borse Dubai, was created to own both DIFX and the Dubai Financial Markets.

[18] Establishment of the Emirates Securities and Commodities Authority (ESCA) by virtue of Federal Law No. 4 of 2000.

[19] ECSA also regulates the Abu Dhabi Securities Market.

land deals conducted by members of the DIFC board (interviewees 8 and 9; *Financial Times*, 28 June 2004; 13 July 2005). After pressure from the DFSA board, the then Crown Prince decided to pass the legislation that granted the DFSA substantial independence as well as placing the DIFC under its own separate legal system, modelled on Anglo-Saxon structures and principles (interviewees 8 and 9).

The result was that Law No. 9 of 2004 in respect of The Dubai International Financial Centre was enacted on 13 September 2004. It set out the powers and functions of the DIFC, including the DFSA. It gave the DFSA considerable legal or formal autonomy and powers. Thus it gave the DFSA its own legal personality, allowing it to sue (and be sued).[20] It made the DFSA the sole body responsible for the regulation of financial services in the DIFC and able to carry these out 'without interference from any other body' and accountable only to the DIFC president/governor who is appointed by decree by the Emir of Dubai. The DFSA is headed by a regulatory council appointed for fixed terms and only open to dismissal for cause in accordance with the DIFC's laws and regulations. The council is responsible for supervising the DFSA and managing its executive. The DFSA's tasks include proposing legislation to the DIFC's president, making policies, issuing regulations and carrying out 'solely and in an independent manner the licensing, registration and supervision' of DIFC establishments.

Interestingly, Qatar followed Dubai in establishing the Qatar Financial Centre (QFC) in 2005.[21] It included an IRA for financial services, the QFC Regulatory Authority (QFCRA). The provisions were very similar to those in Dubai, and the QFCRA enjoys considerable legal independence and powers.[22] Such similarities were perhaps not accidental as, following his exit from the DFSA, Philip Thorne went on to head the Qatar authority. However, unlike Dubai, Qatar did not establish a separate international stock exchange but instead is seeking to develop the Doha exchange, which it had set up in 1995–7, notably by allowing non-Qataris to buy up to 25 per cent of companies quoted on the Doha exchange in 2005. Qatar is following the British FSA model to a greater extent than other GCC countries by creating a new single unified financial regulator in 2008 that will oversee all financial services, including banking, and will take over the central bank's existing units and the

[20] See Article 7 for many of the specifications about the DFSA.
[21] See Law No. 7 of 2005, On the promulgation of Law for the Qatar Financial Center,
[22] Indeed, in some respects it has greater independence; for example the provisions on the dismissal of board members are more specific than those for in Dubai.

QFCRA (*Financial Times*, 17 July 2007; *Middle East Economic Digest*, 14 September 2007).

Saudi Arabia has also set up an agency to regulate financial services, the Saudi Arabia Capital Markets Authority (CMA), created in 2003.[23] It followed concerns that the United States was no longer as good a destination for Saudi investments, especially after 9/11, and the creation of the Saudi Stock Exchange as a corporate body, separate from the Saudi Arabian Monetary Agency (SAMA), the country's central bank (*Financial Times*, 22 August 2002; *Middle East Economic Digest*, 14 November 2003). The institutional design of the CMA took elements of the British FSA and the US Securities and Exchange Commission (SEC). Hence the CMA is a government organization, headed by a board of five full-time persons, each appointed for a fixed term of five years, renewable once. It has legal personality, powers to issue rules and regulations, and legally specified duties to ensure the development and proper functioning of the exchange. But the extent of delegation and internationalization is less than in Dubai and Qatar; the CMA reports to the prime minister, and its members must be Saudi nationals. Equally, there has been no move to introduce a separate legal system.

While Dubai, Qatar and Saudi Arabia have radically reformed their regulatory institutions by establishing sectoral IRAs, other GCC countries have followed different paths. Bahrain has chosen to reform securities regulation and move away from self-regulation, but has chosen a supervisory model based on the central bank being a single regulator for the entire financial sector. Thus in 2002 responsibility for supervising the Bahrain Stock Exchange and the insurance sector were transferred from the minister for commerce and agriculture to the Central Bank of Bahrain (CBB, then called the Bahrain Monetary Agency).[24] However, the CBB is not separate from the Bahrain Stock Exchange, as its head sits on the Bahrain Stock Exchange board. Nor is it formally independent from the government: despite new legislation in 2006, its board includes a representative of the ministry of finance.[25]

There were several reasons why Bahrain chose not to create an IRA for securities. One is that no single dominant international model had yet developed in the period 1999–2002, when reforms were being debated (interviewee 15). The British

[23] Royal Decree No. (M/30) dated 2/6/1424 AH (16 June 2003).

[24] Decree Law 21/2002 with respect to the amendment of some articles of Decree Law 4/1987 with respect to the establishment and organization of the Bahrain Stock Exchange.

[25] Central Bank of Bahrain and Financial Institutions Law 2006, Art. 5.

FSA was new and not yet tested, and indeed a single European institutional model had not emerged. There were alternative models and, instead, Bahrain looked at Singapore, where the Monetary Authority of Singapore – the central bank – supervises the entire financial services sector. Policymakers argued that Singapore was a good example for Bahrain, in terms of becoming a dominant regional financial centre and enjoying rapid economic development using human capital and despite lacking natural resources. However, a second factor was the strong resistance by the CBB to losing any of its powers, a position that was supported by the Prime Minister and the Crown Prince. A third reason was that Bahrain has a strong banking sector but a much smaller securities one, and hence there seemed good reasons to keep regulation of the two together. Finally, the central bank argued that establishing a separate IRA for securities would have meant duplication, higher costs and, perhaps more importantly, finding skilled staff. In any case, the government and the CBB invited the IMF and the World Bank to assess the position. Its report in 2006 was largely favourable towards the central bank's regulatory activities, although it noted that the CBB should obtain greater formal independence from the government (this was before the law of 2006) (IMF 2006a, esp. pp.13–16). Moreover, Bahrain joined IOSCO, which validated the model of the CBB as regulator. Hence while international pressures favoured the separation of operations and regulation, they did not point unambiguously to creating an IRA, while domestic actors favoured a powerful central bank.

Kuwait offers an interesting counter-example to the other states. It illustrates the obstacles to reform and the importance of both central leadership and the perceived economic necessity for the creating of powerful IRAs. Kuwait had the oldest GCC stock market, the Kuwait Stock Exchange (KSE). Since the reforms of the early 1980s the KSE has been regulated by a Market Committee, but this is not an independent body; instead, it includes several representatives from the government and, indeed, from the regulatee, the KSE.

There have been powerful pressures to reform the regulatory system, including creating an IRA. The Central Bank of Kuwait and the finance ministry wish to develop the KSE, while the former faced problems because of being responsible for many financial suppliers (interviewees 1 and 3). They invited the World Bank and outside consultants (McKinsey and the International Securities Consultancy (ISC)) to undertake studies in order to gain outside support for change (interviewees 1, 3 and

5). The 2004 World Bank report argued that the Market Committee was inadequate, saying that it ‘has not been delegated appropriate powers and responsibilities to enable it to act as an independent regulatory agency or to oversee the development of an efficient, fair and transparent securities market’ (World Bank, 2004, p. 5). A report by the IMF in 2006 again criticized regulatory arrangements for the stock exchange and repeated the call for reform, suggesting ‘establishing comprehensive oversight of the stock exchange’ (IMF 2006b and more generally IMF 2006c). Similarly, the consultants recommended reform and pointed out that Kuwait’s regulatory institutions were insufficient (interviewees 3 and 6). Another pressure for change was the desire to meet IOSCO’s requirements concerning the independence of the regulator, which the Market Committee did not. Moreover, the KSE has faced the danger of capital outflows, as large investors and companies have been switching their investments to other GCC stock exchanges and it has attracted fewer international investors than other exchanges. One reason for this is believed to be the weaknesses of supervision in Kuwait, especially its not meeting international standards (interviewees 1, 3 and 7; *Emirates Business*, 24/7, 6 October 2008). Finally, there was considerable domestic discontent when, following a large-scale boom, there was a sharp crash in 2005–6, when allegations of market manipulation were made (interviewee 1; *Zawya*, 8 Noveember 2007). There is recognition that an IRA is needed because of the Market Committee’s lack of sufficient independence from the KSE and the fact that its members may face a conflict of interest between their roles as regulators and as market participants (interviewees 3 and 6).

In response to these pressures Kuwaiti policymakers – notably the ministry of commerce, the central bank and the KSE’s leadership – began discussing the creation of an IRA in 2005. Detailed legislative proposals were made by an academic, Dr Amani Bouresli, from the University of Kuwait. Her proposals envisaged a Capital Market Authority, closely modelled on the US SEC and the British FSA (interviewee 1). They also suggested that the CMA should be headed by a board of Kuwaiti citizens appointed for terms of five years, renewable once, with removal being difficult, and that it would have strong powers, notably to punish malpractice, and its own budget, funded by the government. The KSE leadership is also keen to ‘catch up international standards’ and adopt ‘best practice’,[26] and commissioned a report from

[26] Quotations are from interviewees 3 and 5; interviewee 4.

ISC which also recommended an IRA. The legislative committee of the parliament began to look at proposals.

Yet despite these forces in favour of an IRA, no legislation had been passed by August 2008. One reason was the plethora of proposals – no fewer than five were made to the legislative committee as the KSE and other reformers failed to agree a common position and the Kuwait government did not offer a strong lead. But another reason was the strong opposition to reforms by brokers who feared that the new rules would be too strict (interviewees 3, 4 and 5; *Zawya*, 8 November 2007). Finally, the parliamentary system, involving considerable debate and opportunities for delay, has made progress slow. As a result, legislative proposals are still being discussed in December 2008.

In conclusion, several GCC states have moved or are moving towards regulatory agencies for stock exchanges. But there have been important national differences. The institutional forms of agencies differ, with some agencies lacking sufficient independence to qualify as IRAs. Moreover, alternative institutional models to agencies have been followed, notably by Bahrain and Kuwait, which do not have IRAs for their stock exchanges.

The internationalization model seems best suited to explain this pattern. International factors have been crucial for change. The desire to attract overseas investors by establishing new institutions has been a central element in the strategies of GCC policymakers. Moreover, overseas examples and international organizations have provided models, norms and impetus for reform. They have aided the development of reform coalitions and the adoption of institutions that differ radically from the small, informally regulated exchanges that until very recently were seen in GCC states. However, those international factors have interacted with domestic ones. Thus while overseas examples have been important for change, their effects have been mostly in the form of selective learning from abroad, as national policymakers chose the examples from which to learn. As for international organizations, they have often been invited to provide advice, which has usually supported the strategy of GCC leaders. In addition, international norms have been sufficiently flexible to accommodate different institutional arrangements (e.g. the IOSCO norms were compatible with both IRAs and regulation in Bahrain by a non-independent central bank). Moreover, the analysis shows that a suitable domestic environment is essential for reform. Indeed, the case of Kuwait would seem to indicate a paradox: a stronger elected legislature and more scope for political contestation has led to barriers to institutional reform. In contrast, where strong political leadership has been present, notably from unelected rulers, institutional change has been more rapid. Overall, whilst reforms cannot be understood without the analysis of international factors, the role of domestic factors has been considerable and has resulted in considerable variations among GCC states.

3.2. The spread of IRAs in telecommunications

IRAs for telecommunications have been established in several GCC countries. One common reason has been to deal with liberalization – both attracting overseas capital and offering a body separate from the government that would appear to have greater impartiality and expertise in dealing with issues arising from liberalization, such as interconnection and the selection of licence bidders. Another factor has been international norms and organizations. Yet, as with stock exchanges, neither explanation is sufficient on it own; although international examples and norms of having an IRA create significant pressures, these are not always overwhelming, and several GCC states have not created telecommunications IRAs, nor are IRAs essential for liberalization, as the cases of Saudi Arabia and Kuwait will show. A fuller explanation of the changing patterns of governance of telecommunications must look at the interaction of international factors with domestic politics and policymaking. This section examines how and why international factors such as learning and the desire for inward investment have led to the establishment of IRAs in states such as Bahrain and the UAE. In contrast, there are several cases in which domestic factors have prevented the creation of an IRA. It finds evidence that when there is lengthy parliamentary involvement, reforms can be held up or blocked, as in Kuwait, repeating the paradox seen in relation to stock exchanges that stronger and more independent legislatures can hold up the establishment of IRAs.

Debates about IRAs must be placed in the context of wider institutional change in telecommunications. Until the 2000s telecommunications services were a state legal monopoly in GCC countries. They were usually supplied by a government ministry, often the posts and telecommunications ministry. The same ministry would also hold regulatory powers over the sector, notably licensing. However, since there was a public monopoly and few services, the main service being fixed line telephony, those powers were largely unused.

However, international and domestic factors have led to major changes in the governance of telecommunications markets. IRAs have been set up in two GCC states. The first to establish an IRA was Bahrain in 2002, followed by the UAE (which regulates telecommunications at the federal level) in 2003.[27] In formal institutional terms these are IRAs: they have legal powers and personality, their heads are appointed for a fixed term and are difficult to dismiss and they enjoy their own funding, often from licence fees. In institutional terms the governments retains power, but this is often to appoint the board of the IRA.

Several reasons lie behind the decision to create an IRA. One has been overseas examples. By the 2000s, all EU countries and many others, from Latin America to south-east Asia, had a telecommunications IRA (Thatcher, 2002; Levi-Faur, 2003). Other Arab states began to establish them (e.g. Jordan in 1995 and Egypt in 2003). GCC states looked to overseas examples, both directly and through consultants and importation of foreign experts. The similarities between several GCC IRAs and those in Western countries, especially the United Kingdom, are striking. The IRAs are usually given legal personality, including the ability to sue and be sued. They consist of a board of several members; sometimes they are have a director general (the equivalent of the chief executive officer of the British communications regulator, Ofcom). Those members cannot be dismissed except for reasons generally specified in the governing law, such as criminal conviction, misconduct or ill-health.[28] The law sets out the IRA's duties, which cover both competition and such objectives as achieving some form of 'universal service' and developing telecommunications activities.[29] These bear strong similarities to the list of duties given to Britain's telecommunications IRA, Oftel, in the 1984 Telecommunications Act (see Thatcher, 1999).

In addition, international norms created incentives for setting up an IRA. The WTO agreements on telecommunications and information technology were signed by several GCC countries by the mid-2000s (*Financial Times*, 22 June 2005).[30] The

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[27] Federal Law by Decree No. 3 of 2003, Telecom Law.

[28] See e.g. for UAE, Federal Law by Decree No. 3 of 2003, Telecom Law, Art. 11.

[29] See e.g. Chapter 2 Art. of the Qatar Telecommunications Law of 2006, or Art. 7 of Oman's Telecommunications Act of 2002.

[30] Thus Bahrain and Saudi Arabia, for example, have signed the WTO Information Technology agreement, while Oman joined the WTO in 2000 and hence signed the WTO telecommunications services agreement, making commitments to liberalize the entire sector, to ensure arrangements that allowed fair and effective competition, notably involving interconnection, and having an independent

United States has put pressures on GCC states to alter governance arrangements (interviewee 13; *Financial Times*, 22 June 2005); one element has been the signature of bilateral free-trade agreements with the United States.[31] These agreements specify, in language similar to that of the WTO, that both sides must have an IRA which must act impartially; equally, they stipulate privatization of operators and insist on allowing competition and the development of rules to ensure that competition is fair.[32]

A third reason for the spread of agencies has been the liberalization of telecommunications markets. Within GCC states demand has been growing for new services from both households and businesses, especially for financial services which have become a priority sector for many GCC states (interviewee 13). Moreover, new services have emerged that can be more easily opened to competition than fixed line telephony, notably mobile services, which then needed regulation.[33] Even fixed line services are being opened up to competition.[34] An IRA is useful in dealing with liberalization by offering an impartial body which also has the technical expertise to deal with issues that may be politically difficult and/or purely technical, such as interconnection costs or tariffs. Such a body, separate from government, is especially valuable in GCC countries, since incumbent telecommunications operators remain state-owned (interviewee 13).

A fourth reason, closely related to liberalization, has been the desire to attract inward investment, especially in new services. Third-generation mobile services provide the clearest example: almost all GCC states have encouraged overseas bidders for new licences. Many bidders have been telecom companies based in other GCC states – for instance, in Oman, the second mobile licence has been award to the Qatari

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regulator that was ‘separate from, and not accountable to, any supplier of basic telecommunications services’. See WTO (2000).

[31] For instance by Bahrain in 2004 and by Oman in 2005.

[32] See e.g. Art. 12(7) of the Agreement between the Government of the United States of America and the Government of Bahrain on the Establishment of a Free Trade Area, which states that ‘Each Party shall ensure that its telecommunications regulatory body is separate from, and not accountable to, any supplier of public telecommunications services’, ‘Each Party shall ensure that the decisions and procedures of its telecommunications regulatory body are impartial’, and ‘Each Party shall maintain the absence of or eliminate as soon as feasible national government ownership in any supplier of public telecommunications services’.

[33] Thus, for instance, in Kuwait the number of mobile subscribers rose from 21.74 per 100 inhabitants in 2000 to 91.49 in 2007, and in Bahrain from 30.61 to 122.88. Similarly, the number of internet subscribers rose very sharply, e.g. in the UAE from 6.45 per 100 inhabitants in 2000 to 20.64 in 2007 (see Appendix).

[34] Thus, for example, the UAE sold a second fixed licence in 2005, which was won by du, offering a fixed line alternative to the incumbent Etisalat since 2006; Saudi Arabia is also opening up its fixed line market.

Telecommunications Company (Nawras) while the third-generation mobile licence in Kuwait was awarded in November 2007 to Saudi Telecom. Several bids, however, have involved consortia of Middle-Eastern and Western companies.[35] An IRA is able to handle competing bids and can be seen to be impartial. It can increase the credibility of state commitments in the eyes of overseas entrants, who can worry either that their bids will not be fairly treated or that regulatory conditions will change once they have made their investment (Levy and Spiller, 1996).

The policies of Gulf states in telecommunications have therefore changed, in ways similar to those for stock exchanges. They seek the creation of a well-functioning telecommunications market as part of wider strategies of attracting inward investment and economic development, both in the telecommunications sector and in other strategic sectors such as finance. They have therefore ended monopolies and sought to create regulators that are seen as impartial. They have given licences to overseas operators – both from other GCC states and from outside. In addition, their own incumbent operators have expanded abroad, especially in other GCC states, through overseas subsidiaries, the purchase of overseas operators and taking licences.[36]

The case of Bahrain offers a clear illustration of the reasons for the spread of IRAs in telecommunications. For Bahrain a major question in the 2000s was how to become a business centre in the region in order to increase future revenue (Bahrain has few oil or gas revenues). A key sector is finance, and indeed banks pressed for the liberalization of telecommunications (interviewee 13). The government asked its Economic Development Board to examine the issue, but also invited consultants and an international US-based law firm (White and Case), who recommended an IRA largely modelled on overseas IRAs, notably that of the United Kingdom (interviewees 13, 16 and 17). A key argument was the desire to meet international 'best practice'. Another reason was that Bahrain wished to sign a free trade agreement with the United States as part of a wider political relationship with and recognition by the United States, and that agreement required an IRA for telecommunications (interviewee 17). The policy obtained support from the highest level. Indeed, the overall strategy of liberalization and institutional reform was strongly supported by

[35] E.g. Vodafone in Bahrain, or the Nordic operator TDC as part of Nawras in Oman.

[36] Examples include Etisalat, which has licences in other GCC states but has also bought stakes in other operators, e.g. the Pakistani operator Pakistan Telecommunication Company Limited in 2005.

the Crown Prince, who emphasized the importance of attracting international investment and telecommunications providers (Interviewee 16).

As a result, the Telecommunications Regulatory Authority (TRA) was created in 2002 as an independent legal entity.[37] The approach ‘very much followed UK thinking’, as Britain was seen as having a well-developed regulatory system that was more appropriate than the US system, which was seen as too convoluted and lacking flexibility (interviewee 17). The TRA’s duties and powers were remarkably similar to those of the British IRAs, notably the telecommunications regulator Oftel and its successor Ofcom.[38] Thus, for instance, the TRA was given duties of protecting the interests of subscribers and users over tariffs, ensuring service provision, quality of service and protection of privacy, promoting effective and fair competition and ensuring that licence applicants could provide the services for which they were applying. It was given powers to enforce the law, notably to ensure compliance with licences and to review tariffs. Equally, the TRA’s structure has strong similarities with the chief executive and board structure used by Ofcom since 2000. Thus the TRA’s powers are exercised by a general director, who is appointed for a three-year term, renewable only once, with dismissal only being possible for certain specified grounds (such as misconduct) through a decree issued by the Council of Ministers. The TRA is supervised by a board of directors, who are appointed for three- or four-year terms. The TRA has been given a degree of financial autonomy from the government in that it is funded from fees, fines and annual fees on licensees up to 1 per cent of their turnover, and it uses its funding to pay salaries and for operations. The minister’s main role is to set policy through a three-yearly Telecommunications Plan; the TRA is to ‘act in manner that is consistent with the objectives’ of the Plan, provided that this does not derogate from its independence’.[39] Otherwise the minister can only intervene indirectly, such as through appointing the members of the TRA board, who in turn choose the TRA general director.[40] Hence, in formal institutional terms, the TRA has significant separation from the government.

The decision to create the TRA forms part of a wider strategy of internationalization for telecommunications in Bahrain. At the regulatory level, many

[37] Legislative decree No. 48 of 2002, promulgating the Telecommunications Law.
[38] Oftel was the telecommunications regulator in 1984–2000, now replaced by Ofcom, the Office of Communications.
[39] Telecommunications Law, s. 3(e).
[40] In addition, it owns a majority share in Batelco, the incumbent operator.

overseas personnel have taken senior positions within the TRA, thus, for example, the TRA's first general director, Andreas Avgousti, was a former Director of Competition and Fair Trading at the British telecommunications regulator Oftel, while his successor, Alan Horne, had worked for British Telecom and then for a consultancy company in Britain. The TRA's approach has been closely modelled on that of foreign institutions, especially that of Britain – for example, in its approach to competition.[41] It has centred on liberalization and the entry of new overseas companies.[42]

Three GCC states have sectoral agencies that are not IRAs. One is Saudi Arabia, which created the Communications and Information Technology Commission (CITC) in 2001, but left it insufficiently separate from the government to qualify as a fully fledged IRA. In particular, the communications minister chairs the board, which also includes 'representatives' from the PTT, finance and national economy, and commerce ministries. Similarly, Qatar created a specialized agency, ictQatar, in 2004, whose highest body, the Supreme Council for Information and Communications Technology, contains members of the government.[43] However, interestingly, the lack of an IRA has not prevented liberalization. Thus in Saudi Arabia the CITC governor declared in 2004 that its aims were to encourage both foreign and domestic investment and to introduce competition into the sector (interview, Mohammed Al-Suwaiyal; *Middle East Economic Digest*, 23 July 2004, pp. 30–5). Indeed, Saudi Arabia awarded a second GSM (Global System for Mobile communications) mobile licence in 2005 to Mobily, a consortium led by the UAE telecommunications incumbent Etisalat[44] and a third one in 2007 to the Kuwaiti/Bahrain supplier MTC (*Middle East Economic Digest*, 10 August 2007, p. 20). It also began the liberalization of fixed line telephony, involving ten bids for a second licence that led

[41] For example in interconnection or in the emphasis on sustainable competition; see TRA Bahrain Annual Reports.

[42] For instance, the second mobile licence was awarded in 2003 to MTC-Vodafone after a bidding process that saw ten bids, mostly from overseas companies, while two new national fixed wireless service licences were issued in 2006–7 to MTC-Vodafone Bahrain and to Mena Telecom, a subsidiary of Kuwait Finance House (Bahrain).

[43] The 2006 legislation is complex, as although powers are given to both the Supreme Council and the General Secretariat, the Secretary General is to carry out the operations of the Supreme Council; see notably Arts. 2–5 of the Telecommunications Law of 2006.

[44] Etisalat owns 35 per cent, with 45 per cent held by six strategic local partners; the remaining 20 per cent was put up for public subscription in an initial public offering (IPO).

to three bids being recommended, all of them by consortia led by overseas suppliers.[45] The CITC ran the bidding process and made recommendations to the Saudi cabinet (cf. *Financial Times*, 15 July 2004; *Middle East Economic Digest*, 21 and 23 July 2004, 19 January 2007).

The experience of Saudi Arabia is interesting, as it shows that a fully fledged IRA is not essential for policies of liberalization and inward investment. Hence a simple functionalist explanation that the establishment of IRAs follows changing market needs is insufficient. Equally, it shows the extent to which governance of the largest GCC market is developing and the strength of forces for change that apply even in an oil-rich and large country.

The most different case among the GCC states is Kuwait. Telecommunications remain regulated by the ministry of communications. An IRA has been discussed for some time and is strongly desired for several reasons which illustrate the pressures to create IRAs. One factor is the need to attract inward investment and boost investor confidence (interviewee 2). Thus, for instance, Kuwait is undertaking liberalization measures such as seeking bids for a third mobile licence. The need for reform was underlined when Zain (formerly MTC), a large Kuwait-based new entrant with subsidiaries and stakes across the Middle East, announced in September 2007 that it would move the headquarters of its international operations unit from Kuwait to Bahrain; one reason for this may have been difficulties in Kuwait concerning legal regulatory barriers linked to the lack of an IRA (interviewee 13; *AMEinfo*, 19 September 2007; reporting by Reuters, *Arab Times*, 1 October 2007).

Another reason in favour of an IRA in Kuwait is to ensure that the market works properly (interviewee 2). In particular, issues such as interconnection, monitoring of prices and frequency management are difficult, and it is argued that they would be helped by an IRA. (interviewee 2; *Kuwait Times*, 14 November 2007, reported in TMC Net). This need is becoming stronger as more operators enter the Kuwaiti market, notably different operators in mobile telephony. As Gamal Anwar Al-Sadat, the chairman of Easytel, a company advising the Kuwait ministry put it, 'An independent telecommunications authority to regulate the market is the thing that

[45] Consortia led by Bahrain Telecommunications Co., Hong Kong's PCCW and US Verizon Communications (*Financial Times*, 12 March 2007; *Arab News*, 22 April 2007), although at present there is only one fixed licence issued – see www.citc.gov.sa/citcportal/GenericListing/tabid/104/cmspid/{B4A40E7A-F8F8–4C1E–8B15–4DDFC32282DC}/Default.aspx.

makes businesses breathe; the authority is the fair judge between all operators' (*Kuwait Times*, 14 November 2007, reported in TMC Net). A final reason is the desire to meet international norms. Kuwait is the only GCC state without an IRA for telecommunications. As one senior policymaker put it, 'everybody is doing it' (interviewee 2).

Discussions about creating a telecommunications IRA have been going on for some years in Kuwait, and there is little opposition in principle. Yet no IRA has yet been set up. One reason appears to be that ministers have different views. Another may be that Kuwait is not looking at other countries as models or examples (interviewee 2). However, an IRA was planned for the next few months, to coincide with the launch in 2008 of a third mobile network, empowered to implement policy, license services, enforce rules and deal with disputes (*Middle East Economic Digest*, 10 August 2007; *Kuwait Times,* 14 November 2007, reported in TMC Net).

Thus, overall, several GCC states have created IRAs for telecommunications. The desire to attract outside investment and to regulate newly liberalized markets have been significant factors, as well as the influence of overseas examples and international norms and incentives. But other GCC states have established agencies that have only limited formal independence and hence do not qualify as IRAs, while Kuwait has continued with regulation by the posts and telecommunications ministries. The overall pattern therefore suggests that international factors offer incentives and reasons to create IRAs for telecommunications, but that domestic circumstances affect whether and when they do so or instead establish other forms of agency or continue with traditional regulatory structures.

4. CONCLUSION: CHANGES AND CHALLENGES IN THE GOVERNANCE OF GCC MARKETS

The formal institutions of governance of both securities trading and telecommunications markets in GCC countries have been radically reformed. New stock markets have been created, with formalized rules or even their own legal systems. Telecommunications suppliers have been transformed from ministries into legal corporations and supply has been liberalized. Overseas firms have been permitted to enter both stock markets and telecommunications. Most importantly, a central institutional reform has been the establishment of specialized sectoral agencies, and in particular IRAs, to regulate the two sectors.

This paper began by putting forward three explanatory models for the creation of IRAs, namely a national model based on principal–agent theory, a cross-national diffusion model and an internationalization model. Each used different factors to explain why IRAs are created and offered diverse explanations and hypotheses about the spread of IRAs across countries. The national model argues that national policymakers rationally calculate the costs and benefits of creating IRAs. It predicts that IRAs are created to perform useful functions for policymakers, such as enhancing credible commitment or shifting blame. If wider national institutions and circumstances vary, so should the spread of IRAs, as the costs and benefits for national policymakers will differ. The diffusion model suggests that IRAs spread across states through mechanisms such as learning, coercion, modelling and regulatory competition. They will do so across countries with diverse domestic circumstances as cross-national linkages overcome the effects of domestic differences. Finally, the internationalization approach argues that international factors influence the incentives, opportunities and strategies of national policymakers within domestic arenas and hence are crucial in explaining their decisions. But international factors interact with domestic institutions and circumstances, so that their impact on decisions varies.

Which of these approaches best explains the pattern of the spread of IRAs in GCC countries in the case of stock markets and of telecommunications? The analysis suggests that the functional advantages of IRAs for policymakers put forward by principal–agent models of delegation have certainly been a significant factor in reform. The desire to attract international capital by enhancing credible commitment through new institutions appears to have been an important factor. Equally, the need to deal with difficult and technically complex issues such as regulating competition or spectrum management were also present. Other reasons put forward by the principal–agent model seem less important, notably blame-shifting and dealing with demands from international organizations.

However, pressures arising from the desire for enhanced credible commitment or dealing with increased complexity seem to be insufficient conditions for the creation of IRAs. Several countries have sought to attract inward investment and liberalized their markets without an IRA – for instance, Kuwait and Saudi Arabia in telecommunications. Others have found alternative institutional models, such as a central bank regulating stock exchanges (notably in Bahrain). Although there may be pressures to establish an IRA in order to attract overseas capital or deal with complex issues, countries can resist those pressures or find alternative institutional responses. Moreover, GCC states have much capital available to them, whereas the reforms have been aimed at attracting non-GCC investors, indicating that change has been driven by policy choices rather than the simple need to attract capital.

Several of the factors put forward by the cross-national diffusion approach have also played a significant role in the spread of IRAs. Cross-national learning and mimetism or modelling were very important, although coercion and regulatory competition appear to have been relatively limited. It is noteworthy that GCC policymakers looked to Western countries, especially Britain, aided by consultants and senior personnel drawn from there. Moreover, the World Bank and the IMF produced reports urging reforms. Hence many institutional features such as the structure of a board and duties centred on competition were copied into GCC IRAs.

At the same time the analysis shows the limits of overseas examples. First, cross-national learning and mimetism have been selective – GCC policymakers have ‘learned’ when and whence they wished. Hence in securities trading, for example, Dubai and Qatar looked mainly to Britain, whereas Bahrain chose to emulate Singapore rather than western Europe. Second, the World Bank and the IMF were often invited by domestic officials to make reports, and perhaps unsurprisingly, they often produced advice that was close to that desired by the policymakers who had requested them. Thus these reports recommended IRAs in some countries, but not for others (e.g. securities trading in Bahrain). Finally, cross-national learning and mimetism have sometimes been insufficient to lead to change, as some countries have chosen not to follow the example of overseas IRAs or have been unable to because of domestic opposition. Hence, for example, Kuwait has not yet introduced IRAs despite looking to overseas reforms, while Saudi Arabia has chosen to establish agencies that are not IRAs.

Perhaps the most complete explanation of the pattern of governance reform – not just the spread of IRAs, but also other forms of agency and sometimes no agency – is provided by the internationalization approach. This suggests that international factors can play a crucial role in domestic reform but also underlines their interaction with national circumstances. In GCC countries, the desire to attract non-Gulf capital and expertise have provided a rationale for IRAs. Equally, overseas reforms have provided examples to be copied or at least modelled. In addition, the recommendations of international organizations such as the World Bank and IOSCO and free-trade agreements with the United States have aided in legitimating reforms.

But it is important to recognize that these international factors are not decisive on their own. One reason is that international examples are numerous and often ambiguous, and hence are open to selective learning. Another is that they are insufficient to overcome domestic obstacles to creating an IRA. Moreover, institutional alternatives to IRAs exist. Equally, the influence of international organizations has depended on being invited to give advice, which, as seen, usually accords with the preferences of domestic reformers and differs from one country to another.

Hence the impact of international factors is conditioned by domestic strategies and conditions. It varies according to the strategies of national leaders and their ability to overcome domestic opposition. Thus Dubai's strategy of international development based on importing Western institutions such as IRAs stands in contrast with less dependent agencies created in Saudi Arabia, while Kuwait is engaged in a lengthy process of reform that involves several proposals and considerable discussion by the parliament. There is a paradox that Kuwait's relatively more independent legislature that is the subject of contested elections has been an important constraint on the adoption of IRAs, whereas strong leadership by non-elected rulers in other countries has aided the spread of IRAs. Finally, it is perhaps unsurprising that reforms to create IRAs and alter governance institutions have gone furthest in Dubai and Bahrain, which lack oil revenues, whereas they have been more limited and slower in Kuwait and Saudi Arabia, which have massive energy reserves.

This paper has focused on the establishment of formally or legally independent regulatory agencies rather than their behaviour. IRAs are often seen as an essential step towards creating markets bound by predictable rules and organizations. However, once created, they then need to develop in ways that create confidence in non-GCC overseas investors about their future treatment if they are to succeed in attracting such investors. They require sufficient expertise to be capable of regulating complex markets in ways that involve economic, political and social choices. They need to develop a practical autonomy in practice from governments, which can be tempted to intervene for their own short-term interests. Equally, they must be independent of local interests, so that the application of rules is seen to be the same for domestic as for overseas parties. These challenges are common to IRAs across the world, but are stronger for new IRAs and also in countries that lack the traditions and administrative and political institutions for delegating power and separating certain decisions from domestic political and social pressures. Establishing formally independent IRAs can be the first step in a process of developing the rule-bound governance of markets that enjoys a degree of autonomy from short-term domestic interests. The economic crisis that has developed since 2007/8 will test the strength of IRAs and their ability to act independently of governments and domestic interests. More generally, it will open questions about the strategy of attracting outside investment and the role of IRAs in the development of telecommunications and financial markets. If the internationalization analysis offered in this paper to explain how, when and why IRAs have been created applies also to the functioning of IRAs, we can also expect both that international factors will be crucial for the operation of IRAs and that domestic conditions will affect responses to such factors, so that there will be significant variations across GCC nations.

Thus the response to why IRAs and other types of agency have spread in GCC states involves analysing the interaction of international factors with domestic conditions and strategies. International factors can provide impetus and legitimation for institutional changes such as the establishment of new agencies. But they are mediated by domestic factors. The overall result has been a sharp alteration to the formal institutions governing GCC markets but also important differences between GCC states.

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INTERVIEWEES

(The order in which interviewees are given does not correspond to the numbering in the notes.)

Mr Jameel Al-Alawi, Senior Legal Advisor, Economic Development Board, Bahrain
Eng. Abdulaziz M Alosaimi, Under-Secretary, Ministry of Communications, Government of Kuwait
Mr Babu das Augustine, Business Banking Editor, *Gulf News*
Mr Andreas Avgousti, General Director, TRA, Bahrain, 2002–6 (telephone interview)
Dr Amani Bouresli, University of Kuwait
Ms Roberta Darfur, DFSA

Mr Liam Gibbon, Capital Markets Supervision Directorate, Central Bank of Bahrain
Ms Lubna Al Hajri, Vice-President, External Relations, DIFX
Mr Alan Horne, General Director, TRA, Bahrain
Mr Zaal Ibrahim, Corporate Affairs Department, DIFX
Ms Joyce Maykut, QC, General Counsel and Secretary of the Board, Dubai Financial Services Authority
Mr Yousef O. Al-Mejalhem, Financial Controller, KFAS, and advisor to the Committee on Stock Exchange Regulation, Kuwaiti Parliament
Mr Faleh A Al-Raqaba, Deputy Manager for Exchange Market Affairs, Kuwait Stock Exchange
Mrs Wafa Mohamed Al-Rasheed, Director of Technical Bureau Department, Kuwait Stock Exchange
Dr Nasser Al-Sanee, member of the legislative committee of the Kuwaiti parliament
Mr Ali Salman Thamer, Director, Capital Markets Supervision Directorate, Central Bank of Bahrain
Mr Keith Williams, Trading Sector consultant and project manager CMDP, Kuwait Stock Exchange

APPENDIX. DATA ON GCC STOCK EXCHANGES AND TELECOMMUNICATIONS MARKETS

Table 1. Stock exchanges, February 2008

	Year of commencement of stock trading	Name of market, year established	Number of listed companies
Bahrain	1957	Bahrain Stock Exchange, 1987 (operating 1989)	50
Kuwait	1952	Kuwait Stock Exchange, 1977	195
Oman	1988	Muscat Securities Market, 1988	124
Qatar	1997	Doha Securities Market, 1995 (operating 1997)	40
Saudi Arabia	1935	Tadawul, 2001 (organized stock market since 1984)	115
Abu Dhabi	1989	Abu Dhabi Securities Market, 2000	66

Source: Shochat (2008, p. 45).

Table 2. Key data on GCC stock market size and activity, yearly summary

Year	2003	2004	2005	2006	2007
Value traded					
Abu Dhabi Securities Market	3,335.56	26,691.37	17,907.82	42,825.18	
Bahrain Stock Exchange	254.69	413.76	600.96	1,228.91	816.07
Doha Securities Market	1,645.86	25,407.03	0,334.48	24,738.05	
Dubai Financial Market	11,628.46	105,277.66	3,657.37	89,904.85	
Kuwait Stock Market	53,300.18	51,637.18	3,990.64	55,714.14	120,659.30
Muscat Securities Market	1,224.38	1,895.70	2,999.96	2,073.74	4,714.61
Saudi Stock Market	158,567.51	446,898.51	68,216.79	1,331,782.90	628,055.57
Shares traded					
Abu Dhabi Securities Market	651.79	7,834.90	10,371.63	47,599.04	
Bahrain Stock Exchange	368.49	311.77	378.75	663.15	683.84
Doha Securities Market	67.54	934.20	1,869.76	2,761.28	
Dubai Financial Market	4,148.97	24,233.67	39,167.73	92,438.70	
Kuwait Stock Market	48,765.60	33,433.37	50,815.60	35,520.20	66,206.68
Muscat Securities Market	275.98	336.97	399.84	867.62	2,721.80
Saudi Stock Market	5,531.22	9,887.70	10,826.73	53,879.96	53,083.03
Market capitalization					
Abu Dhabi Securities Market	55,519.12	125,646.08	71,688.79	112,159.52	
Bahrain Stock Exchange	9,701.77	13,513.18	17,276.34	21,122.84	26,795.93
Doha Securities Market	40,435.90	87,140.94	60,913.09	95,517.99	
Dubai Financial Market	35,109.07	108,774.68	86,871.72	138,697.83	
Kuwait Stock Market	61,311.56	73,769.25	139,486.14	141,923.18	193,513.28
Muscat Securities Market	6,615.17	–	10,928.07	13,036.98	22,767.03
Saudi Stock Market	157,164.12	305,954.25	647,502.66	326,364.47	522,721.12
Number of transactions					
Abu Dhabi Securities Market	62026	531093	665415	987469	
Bahrain Stock Exchange	14200	14948	20994	16110	24004
Doha Securities Market	70275	1012174	1736160	1524306	
Dubai Financial Market	182094	1644448	2375247	2007151	
Kuwait Stock Market	1066078	1052820	1908475	1397529	1976340
Muscat Securities Market	178163	250873	337959	285737	524019
Saudi Stock Market	3742102	12616825	13283983	12985128	11343727

Source: AMF (Arab Monetary Fund), available at www.amf.org.ae/AMF/WebSite/weblisher/storage/uploads/docs/economic%20dept/amdb%20update/markets%20performance/yearly%20performance/yearly%20summary.htm.

Table 3. Mobile cellular subscribers in GCC countries 2000–7

3.1. Mobile cellular subscribers, 2000

	(000s)		*CAGR (%)*	*Per 100 inhabitants*	*As % total telephone subscribers*
	1995	*2000*	*1995– 2000*	*2000*	*2000*
Bahrain	27.6	205.7	49.4	30.61	54.6
Kuwait	117.6	476.0	32.3	21.74	50.5
Oman	8.1	162.0	82.3	6.63	42.2
Qatar	18.5	120.9	45.6	19.90	43.0
Saudi Arabia	16.0	1,375.9	143.7	6.40	31.7
United Arab Emirates	129.0	1,428.1	61.8	43.98	

3.2. Mobile cellular subscribers, 2007

	(000s)		*CAGR (%)*	*Per 100 inhabitants*	*As % total telephone subscribers*
	2002	*2007*	*2002–7*	*2007*	*2007*
Bahrain	389.0	1,116.0	23.5	148.28	*82.4*
Kuwait	1,227.0	2,773.7	17.7	97.28	*83.0*
Oman	463.0	2,500.0	40.1	96.33	90.3
Qatar	266.7	1,264.4	36.5	150.41	84.2
Saudi Arabia	5,008.0	28,381.0	41.5	114.74	87.7
United Arab Emirates	2,428.1	7,594.5	25.6	173.37	84.6

Source: ITU annual report.

Table 4. Internet development in GCC countries, 2000–7

4.1. Internet development, 2000

	Internet				*Broadband subscribers*	
	Subscribers (000s)	*Subscribers per 100 inhab.*	*Users (000s)*	*Users per 100 inhab.*	*Total (000s)*	*Per 100 inhab.*
Bahrain	21.9	3.25	40.0	5.95	-	-
Kuwait	...	...	150.0	6.85	...	...
Oman	23.9	0.98	90.0	3.69	...	...
Qatar	10.5	1.74	30.0	4.94	-	-
Saudi Arabia	200.0	0.93	460.0	2.14	-	-
United Arab Emirates	209.5	6.45	765.0	23.56	1.4	0.04

4.2. Internet development, 2003

	Internet				*Broadband subscribers*	
	Subscribers (000s)	*Subscribers per 100 inhab.*	*Users (000s)*	*Users per 100 inhab.*	*Total (000s)*	*Per 100 inhab.*
Bahrain	48.9	6.93	150.0	21.25	9.7	1.38
Kuwait	227.0	9.14	567.0	22.82	13.0	0.52
Oman	51.8	2.06	210.0	8.36	0.1	0.01
Qatar	33.3	4.71	140.8	19.93	3.0	0.42
Saudi Arabia	700.0	3.00	1,800.0	7.72	46.0	0.20
United Arab Emirates	347.5	8.60	1,110.2	27.48	30.3	0.75

4.3. Internet development, 2007

	Internet				*Broadband subscribers*	
	Subscribers (000s)	*Subscribers per 100 inhab.*	*Users (000s)*	*Users per 100 inhab.*	*Total (000s)*	*Per 100 inhab.*
Bahrain	60.1	8.14	250.0	33.22	38.6	5.23
Kuwait	283.2	10.54	900.0	31.57	25.0	0.93
Oman	70.3	2.71	300.0	11.56	18.9	0.73
Qatar	87.0	10.34	351.0	41.75	70.3	8.37
Saudi Arabia	1,800.0	7.14	6,200.0	25.07	600.0	2.43
United Arab Emirates	904.0	20.64	2,300.0	52.51	240.6	5.17

Source: ITU annual report.

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